Alberta Petroleum Marketing Commission

APMC

ANNUAL REPORT

FOR THE YEAR ENDING
DECEMBER 31st, 2013

2013 HIGHLIGHTS

APMC faced another challenging year in 2013. It was characterized by a rapidly evolving petroleum market place, ongoing challenges to the development of new infrastructure, and the emergence of numerous commercial proposals to expand market access.

A significant accomplishment in 2013 was the passage of the *Building New Petroleum Markets Act*, which amends the *Petroleum Marketing Act* to modernize it and provide clarity around APMC's governance. The debate on the passage of this Act highlighted the important role that APMC can play in helping Alberta achieve full world market price for its crude oil and bitumen through the development of new infrastructure and new markets. A major step in this direction was the commitment to 100,000 bpd of capacity on the Energy East pipeline that was made early in 2013. The debate also highlighted the important role that APMC is playing in adding value to our resources, through its contract with the Sturgeon Refinery, and through other opportunities that it is evaluating as discussed later in this report.

The development of the Sturgeon Refinery faced significant challenges during 2013. Initial plans to complete the syndicated bank financing and first bond offering in 2013 were deferred. In November, a new cost estimate was completed and the budget for the project was increased to $8.5 billion from $5.7 billion. This cost increase was beyond the capacity of the existing commercial structure, and as a result, APMC stepped forward to play a larger role in the development of the project. The arrangement that was put in place in December removed the cap on capital costs to be paid by the toll payers, and called for APMC and Canadian Natural Resources to each provide up to $350 million of subordinated debt to the North West Redwater Partnership. This would facilitate the partnership successfully accessing bank and bond markets for the 80% senior debt financing that was initially intended. This arrangement gives APMC a temporary 25% voting interest in matters related to the construction, start-up and operation of the Sturgeon Refinery, requiring more involvement in ongoing decision making. Bank and bond financing is now anticipated to be completed by mid-2014.

APMC also made progress on its internal development during 2013. A draft strategic plan was prepared and presented to the Board in Q4. APMC with the Department of Energy developed materials for the Minister to use with her colleagues to clarify APMC's mandate – a potentially diverse field of endeavor. Clarity of APMC's mandate will support the Board and staff in executing on the mandate in 2014 and beyond. Conventional oil marketing and reference price determination operations continued to be delivered effectively, and considerable progress was made towards the replacement of legacy information systems during the year. Importantly, in 2013 several key staff positions were filled with top quality people, which was crucial in increasing APMC's capacity to deliver results.

I would like to thank the Board for its continued support and counsel, staff of the Departments of Energy; Justice; Treasury Board and Finance and others for their ongoing support, and the staff of APMC for their dedication. I look forward to continuing to enhance APMC's capabilities in order to deliver on the mandate that we have been given.

Richard Masson,
Chief Executive Officer
March 14th, 2014

FINANCIAL ACTIVITY

Each month the net proceeds on the sale of the Crown's conventional crude oil barrels are transferred by the APMC to General Revenue. Net proceeds arise from payments from our agents (Nexen and Shell) for the sale of 90% of the royalty volumes and net revenues from APMC's marketing activities related to the remaining 10% of Crown volumes. Our new agency agreements started with June, 2013 production and prices are based on indices versus previously prices were based on pooled sales. These new agency agreements have a two year term.

In 2013 the dollars remitted were up 8.5% while the volumes sold were up 2.6%. Production of Crown conventional crude oil in the province increased 4% year over year. In addition the calculation of royalty volumes is impacted by prices which were up in 2013. See discussion below related to crude oil valuation.

The quarterly dollars and volumes sold (in millions of barrels) for 2013 and 2012 are as follows:

	Q1		Q2		Q3		Q4		Total	
	$ millions	'000 bbls/d	$ millions	'000 bbls/d	$ millions	'000 bbls/d	$ millions	'000 bbls/d	$ millions	'000 bbls/d
2013	459.0	65.9	504.1	66.4	634.8	72.9	532.7	76.7	2,130.6	70.5
2012	583.9	75.9	496.1	71.8	434.0	62.6	450.3	64.6	1,964.2	68.7

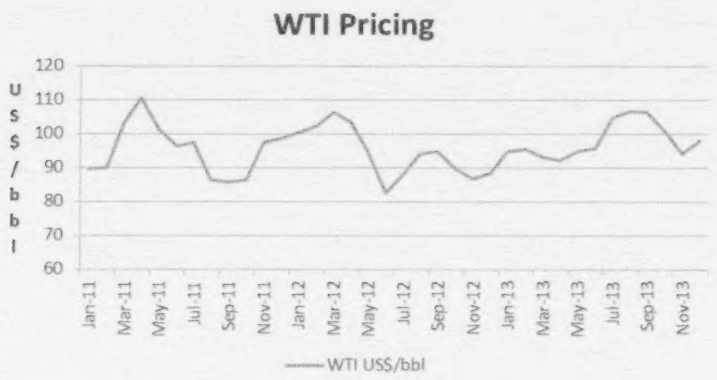
CRUDE OIL VALUATION (SEE APPENDIX A FOR PRICING DATA DETAILS)

The dollars remitted per barrel increased approximately 9% (Cdn $78/bbl in 2012 vs Cdn $83/bbl in 2013).
When comparing the price realizations from 2012 and 2013 we have the following general observations:

- Prices continued to be volatile and crude transportation capacity out of the Western Canadian basin continued to be an issue. This resulted in pipeline apportionment at times.
- Crude prices are quoted in US dollars. A weaker Canadian exchange rate in 2013 (average of 1.03 CAD/USD) versus 2012 (1.00 CAD/USD) resulted in increased prices in Canadian dollars.
- Realized heavy Canadian crude prices in 2013 were similar to 2012 as higher WTI prices and a weaker Canadian dollar were offset by wider heavy differentials.

WTI

- The average 2013 price for WTI was US $97.97/bbl, an increase of 4% versus 2012.
- Global crude prices were lower in the first half of the year due to weaker macroeconomic conditions and increasing supply from North America. The second half of the year saw higher global crude prices mainly as a result of outages in a number of key producing regions including Nigeria, Iran, Iraq and Libya.
- The WTI/Brent differential narrowed through the first three quarters as increased pipeline transportation to the Gulf coast resulted in inventories declining at Cushing where the WTI price is determined. The fourth quarter saw US crude markets disconnecting from foreign markets. Inventories rose in the Gulf coast and both the WTI and Louisiana Light Sweet (LLS) differential to Brent widened.

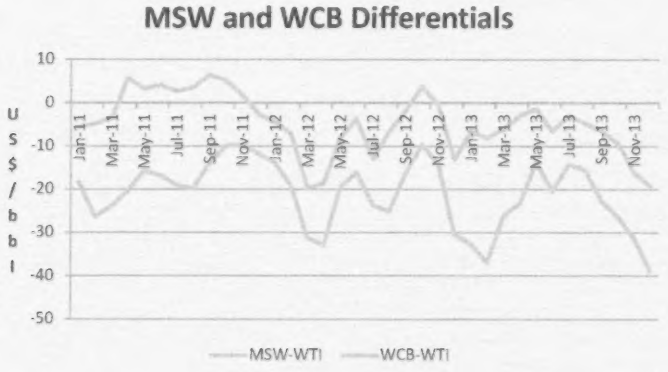


Mixed Sweet (MSW)

- The average realized 2013 MSW price differential to WTI for 2013 was US $-7.91, this level was approximately the same as 2012.
- Volatility was seen during the year in MSW prices. Increased inventory levels and pipeline congestion resulted in wide differentials to start the year in January and to finish the year in the fourth quarter.
- Heavy upgrader maintenance, the easing of pipeline congestion, and increased refinery demand for light crude contributed to a narrower differential during the second and third quarters.
- Longer term takeaway capacity from Western Canada continues to be an issue but future large price discounts should be mitigated somewhat by increased rail loading capacity in Western Canada.

Heavy Differential

- The average realized 2013 Western Canadian Blend (WCB) price differential to WTI for 2013 was US $-25.23, a widening of the differential of US $5.12/bbl versus 2012. Note that WCB is composed of heavy oils, and is a different stream than Western Canadian Select (WCS), which is composed primarily of bitumen with some conventional heavy oils and diluent.
- Similar to MSW, wide differentials were seen in the first and fourth quarters with narrower differentials seen in the second and third quarters.
- Kearl ramping up production, pipeline congestion, refinery maintenance, and several delays starting BP's Whiting coker conversion all contributed to wider differentials from the September to December time period.
- The start of 2014 has seen tighter differentials as the cold weather has impacted supply, more volumes are moving by rail and BP's Whiting refinery has started to increase the volumes of heavy it is taking.



BUSINESS DEVELOPMENT ACTIVITY

APMC continued to identify and analyze business ideas and proposals related to new infrastructure that would allow APMC to access higher-value crude oil demand markets in North America and overseas.

All business development opportunities presented to APMC are being assessed for their strategic value to Alberta, fit within the framework of the Canadian Energy Strategy and ultimately their financial feasibility.

APMC continued discussions and formed new relationships with different overseas marketers and refiners to start laying the groundwork to access new markets for Alberta oil in Asia and Europe.

Some highlights of business development activities during 2013 are listed below:

Pipeline

- APMC completed the evaluation of the proposal from TransCanada for APMC to participate as a Founding shipper in the Energy East pipeline project and received Board approval to sign up for 100,000 bpd of capacity for 20 years with a destination of St. John, New Brunswick. This contract was executed March 21st. The project gained overwhelming commercial support and will be built to its full hydraulic capacity from the outset if it is approved for construction. APMC continues to attend regular Shipper and Executive Committee meetings.
- Evaluated and prepared a business case for a pipeline proposal targeted to access the U.S. eastern gulf coast refining market). The proponents of the project were not able to obtain sufficient commercial support from producers, marketers and refiners through the open season. The project has been shelved indefinitely.
- Evaluated a pipeline project between Edmonton and Hardisty. APMC decided not to participate as the project had adequate commercial support from industry.

Crude by Rail

- APMC engaged with numerous midstream companies for the development of crude oil rail loading facilities in Alberta. APMC did not participate, from a commercial standpoint, in any of the proposals as sufficient industry support was achieved.
- APMC has engaged with industry participants (producers and midstream companies) to advance the development of a Diluent Recovery Unit (DRU) at either Edmonton or Hardisty in order to enable less-diluted bitumen to be shipped in heated and coiled tank cars to North American refineries. APMC believes that this could help to expand markets, improve transportation safety, and offer competitive economics. Talks and analysis will continue through 2014.
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Crude Oil Export Terminal Development

- APMC continues to explore opportunities to export Alberta crude from various Canadian (west/east) and US (west/south) coastal terminals. Social licence issues to the west and economic feasibility to the east/south are the main issues slowing this development. APMC will continue to work with proponents to progress these options through 2014.

Value Add Opportunities

- APMC opportunities are expanding beyond crude oil. We have been presented with opportunities to supply natural gas and propane to facilitate value added petrochemical processing within the province. These potential deals are long term and complex. APMC assessed these opportunities and continues to work with proponents to explore alternate supply arrangements.

Partial Upgrading

- APMC has had discussions with a number of companies who are attempting to commercially develop partial upgrading projects within the province. APMC is interested in supporting these initiatives and will continue to work closely with the technology proponents in 2014.

PRICING AND ANALYSIS ACTIVITY

During 2013, the functions and responsibilities of the business unit covered the following:

- Determinations of the monthly Natural Gas Reference Price and Natural Gas Liquids Reference Prices were completed and delivered to DOE's Gas Royalty Operations for valuation of the Crown share of natural gas and natural gas liquids (NGLs).
- The Crude Oil Par Prices were published by the last day of each month for inclusion in the determination of the Crown royalty share of conventional crude oil for the second month following publication.
- Approvals of claims and statements were made for trucking allowances, equalization assessments, and tariff charges. APMC reimburses battery operators for trucking costs associated with delivering the Crown royalty share to pipelines. Equalization and tariffs relate to quality adjustments and transportation charges on the various pipelines.
- The business unit participated in the Natural Gas Liquids Review, which resulted in changes to the calculation of Natural Gas Liquids Reference Prices. The changes will be effective July 2014 production month. There will be two provincial reference prices calculated for each of propane (C3), butane (C4) and pentanes plus (C5+). One price will be applied to specification grade product (including field condensate) and the other price will be applied to product contained in an NGL mix.
- Each reference price will be a provincial average field price determined from pricing information submitted by NGL purchasers at field facilities in the province of Alberta. Amendments to submissions may result in a restated reference price for the amended production month, unlike the present methodology where amendments are rolled into future months.

SYSTEMS AND PROJECTS ACTIVITY

Much progress was made on the VMS Retirement Project which is going to replace the aging software system currently in use for marketing, accounting and pricing activities. A major new sub-project was identified as Actualization and Settlement (A&S) which will obtain data from RAM (Royalty and Marketing system), Petrinex, and Egistix and complete some calculations and provide this data to the new financial system. The A&S system was at an early stage of development at year end. Business requirements gathering for royalty-in-kind business processes will commence in early February 2014. The following potential solutions have been identified for the finance function: use of IMAGIS (Government of Alberta finance software), modification of CARS2 (DoE finance software used for receivables and revenues), off-the-shelf accounting package, or internally built software. Selection of one of the alternatives will occur in 2014.

The Egistix marketing system generates pipeline nominations for the 10% of Crown royalty barrels marketed by APMC. Enhancements to the system will allow for the tracking of Agent managed Crown barrels and provide that data to the A&S system being developed to replace the current VMS platform.

The Wellhead to Dollars committee is a joint industry and DOE committee mandated to look at ways to improve the end-to-end processes associated with marketing crude oil for both industry and government. The committee members include senior executives from major oil producers and pipeline companies. APMC has actively participated in the oil forecasting assessment phase to provide recommendations to the Steering Committee for industry-wide improvements to the forecasting processes. One of the recommendations brought forward was to propose the development of a Forecast Estimator Tool in Petrinex. The Steering Committee is presenting this proposal to CAPP to provide support for a broader industry consultation to explore the cost/benefits of the tool.

The implementation phase of the Natural Gas Liquids Reference Price Review project started in May 2013. Under revised business processes, natural gas liquid buyers report information to Petrinex and reference prices will be calculated from that information, effective July 2014 production month. An industry work group consisting of natural gas liquid buyers provided valuable input into the design and development of reporting guidelines, which were completed by year-end. A

first draft of required changes to the Natural Gas Royalty Regulation 2009 to support revised reference prices and compliance processes was completed by year-end.

There were significant accomplishments working with DOE's Information Management and Technology (DOE IT) in automating the present Natural Gas Reference Price and the new Natural Gas Liquids calculations. DOE IT has scheduled demonstrations regarding the development of the Natural Gas and Natural Gas Liquids systems commencing February 2014.

PEOPLE ACTIVITY

Grant Sprague took over the role of Chair of APMC from Jim Ellis upon his departure to the Alberta Energy Regulator in July, 2013.In October, 2013 the Executive Director for Petroleum Marketing Valuation and Site Services position was filled.
In November, 2013, the following roles in the Business Development group were filled: Executive Director and Senior Manager.

APPENDIX A – PRICING DATA

Price Realizations Average of Sweet, Sour and Heavy			
	Cdn $ /bbl		
	2011	2012	2013
January	77.65	91.91	75.02
February	74.25	88.51	73.02
March	87.21	79.93	77.85
April	97.67	76.34	79.24
May	91.93	81.33	88.81
June	87.77	75.59	83.82
July	84.80	70.99	97.81
August	76.83	76.61	97.82
September	81.32	82.94	90.58
October	84.55	84.59	81.34
November	94.52	78.19	71.76
December	93.83	65.12	71.41
Average	86.03	79.34	82.37

WTI Calendar Month Average			
	US $/bbl		
	2011	2012	2013
January	89.58	100.32	94.83
February	89.74	102.26	95.32
March	102.98	106.21	92.96
April	110.04	103.35	92.07
May	101.36	94.72	94.80
June	96.29	82.41	95.80
July	97.34	87.93	104.70
August	86.34	94.16	106.54
September	85.61	94.56	106.24
October	86.43	89.57	100.55
November	97.16	86.73	93.93
December	98.58	88.25	97.89
Average	95.12	94.21	97.97

WCS Differentials US$/bbl			
	2011	2012	2013
January	-18.40	-13.85	-32.71
February	-26.33	-19.22	-36.92
March	-23.85	-31.20	-26.24
April	-20.34	-32.94	-23.20
May	-15.70	-19.61	-13.87
June	-16.87	-16.04	-20.41
July	-19.03	-23.65	-14.20
August	-19.83	-25.13	-15.57
September	-14.01	-16.39	-22.67
October	-9.89	-9.69	-26.34
November	-9.84	-14.27	-31.31
December	-11.72	-30.37	-38.94
Average	-17.15	-21.03	-25.20

Mixed Sweet Differentials US$/bbl			
	2011	2012	2013
January	-5.61	-4.49	-6.63
February	-4.94	-7.14	-8.14
March	-3.53	-19.86	-6.08
April	5.76	-18.53	-2.96
May	3.24	-8.11	-1.36
June	4.04	-3.71	-6.68
July	2.69	-12.99	-2.90
August	3.58	-6.74	-4.73
September	6.37	-1.89	-6.54
October	5.20	3.74	-9.30
November	1.76	-0.56	-16.18
December	-2.67	-13.15	-19.31
Average	1.32	-7.79	-7.57